The Energy Improvement and Extension Act of 2008: Investing in the Green Economy Through Renewable Energy Tax Credits, Tax-Exempt Bonds and Green Building Incentives

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Throughout the 2008 Presidential campaign, every candidate talked about the importance of investing in clean and renewable energy as a means of moving the country from dependence on foreign oil, reducing greenhouse gas emissions, and creating millions of jobs in the so-called "green economy." Congress has taken the first step towards achieving those goals with its passage of the Energy Improvement and Extension Act of 2008 (the "Act")[1] as part of the $700 billion bailout package signed into law by President Bush on October 3, 2008.

Among other things, the Act amends the Internal Revenue Code (IRC)[2] to 1) extend and enhance tax credits for renewable and cleaner energy facilities; 2) introduce new clean renewable energy bonds; 3) provide a variety of incentives for biofuels and other cleaner transportation fuels; 4) provide preferential tax treatment for transmission facilities; and 5) add tax credits for energy efficiency initiatives and green building.[3] This **Stroock Special Bulletin** discusses these five main areas of the Act and examines their implications for the renewable energy markets and the green economy generally.

Tax Credit Extensions and Enhancements for Renewable Energy

The Act extends placed-in-service dates, investment tax credits and production tax credits for a variety of clean and renewable energy resources, including wind, refined coal, biomass facilities, marine renewables (waves and tides), and, of course, solar. The extensions of credits for solar and wind are the most notable at present, as they will have the most significant short-term effect on the renewable energy markets.

Investment Credits

The Act provides a significant three-fold boost to the solar industry: 1) extending, until January 1, 2017, the 30% solar investment tax credit for both residential and commercial solar installations, originally enacted in 2005 in Section 48 of the IRC; 2) removing the $2,000 credit cap on residential solar electric installations; and 3) permitting a full tax credit for utility-scale installations. The utility-scale tax credit is particularly important for solar energy development in California and other states in the southwest where large solar installations are most feasible. In California, for example, in response to requirements under California's Renewable Portfolio Standard, utilities have teamed with solar companies to develop large utility-scale operations of up to 350 MW.

The Act also extends for eight years the current 10% investment tax credit for microturbines of less than 2 MW in size and the 30% credit for fuel cells, as this equipment is compatible with smaller-scale renewable electricity generation. The Act leaves in place the current credit cap of $200 per kilowatt of capacity for microturbines, but increases the originally defined fuel cell cap from $500 to $1,500 per half kilowatt of capacity. The Act also extends the 10% credit for geothermal systems for eight years. Finally, the Act creates several new investment credits in Sections 48 and 25D of the IRC:

- a 10% credit applicable to combined heat and power systems under 50 MW;
- a 30% credit capped at $4,000 for small wind energy systems less than 100 kilowatts or located at a residence; and
- a 30% credit capped at $2,000 for residential geothermal heat pumps.

Congress has long been concerned with finding ways to reduce emissions from coal-fired facilities. To address those concerns, the Act amends Sections 48A and 48B of the IRC and adds a new $1.5 billion investment tax credit program providing a 30% credit for certain advanced coal and coal gasification projects with 75% effective carbon capture and sequestration (CCS) systems. This credit program will take effect after the Department of Energy promulgates regulations and will be available for up to six years after such promulgation.

Production Credits

The Act is not as generous towards the wind industry as it is towards the solar industry, perhaps because of the view that wind energy has penetrated the market more significantly than has solar and consequently has less need for further tax credits. The Act only extends for one year, until January 1, 2010, the placed-in-service date for the production tax credit for wind contained in Section 45 of the IRC, and leaves unchanged the generally applicable credit of 1.5 cents per kilowatt-hour of electricity produced for ten years. The Act also extends for two years eligibility for the production tax credit for electricity production from other renewables, including solar, biomass, geothermal, hydro, and the recently added marine renewable resources. To qualify for this production credit, these generation facilities must be placed in service prior to January 1, 2011.

Congress also extended for one-year eligibility for the production credit for refined coal (a liquid, gaseous or solid fuel produced from coal) while doubling from 20% to 40% the amount of emissions reduction required for qualification as a refined coal facility. Production credits for CCS were added in new Section 45Q of the IRC in the form of $20 per metric ton permanently sequestered in secure geologic storage and $10 per metric ton used for enhanced oil and gas recovery. It remains unclear as to whether the investment credits for coal coupled with these production tax credits will be sufficient to stimulate technological innovation that will make CCS cost-effective. Because national carbon regulation will disproportionately affect coal-fired facilities, and thus coal producing states, it may fall to coal producing states to provide additional funds for research in this area.

New Clean Renewable Energy Bonds ("CREBs")

The Act adds new Section 54C to the IRC, which authorizes $800 million of new CREBs to finance the production of "clean" electricity. The funds raised from these bonds will be used to create facilities capable of generating power from wind, biomass, geothermal, qualified hydropower, landfill gas, marine renewable and trash combustion facilities. The new CREB funds will be allocated for qualifying projects as follows:

- 1/3 for state and local governments;
- 1/3 for public power providers (*e.g.*, utilities); and
- 1/3 for electric cooperatives.

The Act also provides a one-year extension for the termination of existing CREBs.

Transportation Fuels

The Act amends Section 40 of the IRC, extending the tax credit for the production of biodiesel fuel (including diesel fuel created from biomass) and fuel produced though coal gasification or liquefaction with CCS. Under this amendment, the current $1.00 per gallon production tax credit and the 10¢ per gallon credit for small biodiesel producers are extended through 2009 and the credit is available for any diesel fuel created from biomass in the United States, without regard to manner in which it is produced, provided the fuel can be utilized by consumers for home heating oil, vehicles, or as aviation jet fuel.

The Act also amends Section 168 of the IRC to replace the available 50% bonus in depreciation of production facilities for "cellulosic biomass ethanol" with the same benefit for "cellulosic biomass." This seemingly minor change removes the exclusive benefit for ethanol. To further increase the incentives for alternative fuel production, the Act extends the 30% credit for building alternative refueling stations through 2010.

On the electric car side, the Act adds new section 30D to the IRC, establishing a $2,500-$15,000 credit for plug-in vehicles, depending on the weight of the vehicle. The credit is to be phased out after 250,000 of such vehicles have been sold in the U.S. The Act also recognizes the importance of "pedal power" by amending Section 132(f) of the IRC to allow employers to provide bicycle storage and maintenance as a fringe benefit.

Sale of Electric Transmission

The Act amends Section 451 of the IRC to extend the current provision allowing for deferral of capital gains on sales of utility-owned transmission facilities to independent transmission companies until January 1, 2010. Instead of having to recognize all the gain in the year of sale, the provision allows utilities to spread out the gain over eight years. It is hoped that this deferral of capital gains will facilitate the sale of transmission facilities, thereby encouraging private investment in new and expanded transmission capacity and increased electric generation from renewable energy resources.

Energy Efficiency and Green Building

Finally, the Act introduces a number of new measures (and extends some current credits) that illustrate the commitment of Congress to energy efficiency and green building to reduce energy costs and lower GHG emissions. The Act establishes a new program in Section 54D of the IRC for qualified energy conservation bonds for capital expenditures that

- reduce energy consumption in public buildings;
- implement green community programs;
- develop alternative and renewable energy sources; or
- promote mass commuting facilities.

The bonds carry with them an annual tax credit of 70%, as calculated under Section 54A(b) of the IRC.

The Act also renews through the end of 2009 the tax credit for residential and non-business energy property expenditures contained in Section 25C of the IRC and which expired at the end of 2007, and extends the credit in Section 179D of the IRC for energy efficient commercial buildings through 2013. Under Section 25C, the tax credit is 10% for energy efficiency improvements to a building envelope, including the installation of green or cool roofs, plus the cost of energy efficient equipment such as high efficiency boilers and HVAC systems. Under Section 179D, the credit for energy efficient commercial buildings is $1.80 per square foot.

The Act includes several provisions that set forth stringent standards for new energy efficient household appliances and higher tax credits for purchasers (*see* Section 45 M of the IRC). The Act also provides for accelerated depreciation of qualified smart electric meters and smart electric grid systems (*see* Section 168 of the IRC). The accelerated depreciation for electric grids is intended to encourage the installation of much-needed state-of-the-art transmission facilities, which may facilitate the transmission of electricity generated by renewable resources to energy constrained areas of the country. President-Elect Obama has said investment in a nationwide smart grid is one of his highest priorities, along with further investment in the development of renewable energy resources.

Lastly, the Act extends to the states and municipalities the authority to issue tax-exempt bonds for qualified green building and sustainable design projects. The extension of this authority, which expires at the end of fiscal year 2012, further demonstrates the federal government's commitment to green building. To be eligible for tax-exempt treatment under Section 142(l) of the IRC, the development project underlying such bonds must be LEED certified,[4] utilize brownfields property, and have local financial support of at least $5 million in the way of tax abatements and contributions-in-kind.

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1. H.R. 1424; together with the Emergency Economic Stabilization Act of 2008, Public Law No. 110-343 (110th Congress, 2nd Session 2008).
2. 26 U.S.C. Subtitle A, Chapter 1, Subchapters A and B.
3. The credits extended or established in the Act are creditable against the Alternative Minimum Tax.
4. Leadership in Energy and Environmental Design standards developed by the U.S. Green Building Council.

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